**BEFORE**

**THE PUBLIC SERVICE COMMISSION**

**OF SOUTH CAROLINA**

**DOCKET NO. 2018-319-E**

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| **IN RE:** | Application of Duke Energy Carolinas, LLC for Adjustments in Electric Rate Schedules and Tariffs and Request for an Accounting Order | **Post-Hearing Brief of The South Carolina Office of Regulatory Staff** |

## I. INTRODUCTION

Pursuant to S.C. Code Ann. Regs. 103-851, the South Carolina Office of Regulatory Staff ("ORS") respectfully submits this Post-Hearing Brief to address the contested issues litigated before the Public Service Commission of South Carolina ("PSC" or "Commission") during the merits hearing held in this Docket on March 21, 2019 through March 27, 2019.

## II. STATEMENT OF THE CASE

Duke Energy Carolinas, LLC ("DEC" or "Company") filed the Application of Duke Energy Carolinas, LLC for Adjustments in Electric Rate Schedules and Tariffs and Request for an Accounting Order ("Application") on November 8, 2018. After considering the proposals sought in the Company's Application, ORS respectfully requests the Commission adopt the following recommendations:

1. Allow DEC to increase Base Facility Charges ("BFC") to recover no more than 25% of any approved revenue increase assigned to the residential time-of-use ("TOU"), residential non-TOU, and small general service ("SGS") rate classes; however, ORS

does not oppose the Company's position[1] of capping the BFC at $11.96 for residential non-TOU customers, $13.09 for residential TOU, and $11.70 for SGS customers

2. Disallow a return on deferred Operation and Maintenance expenses and approve ORS's proposed amortization periods for accounting deferrals;
3. Disallow recovery of $2,399,000 in Operation & Maintenance Expenses;
4. Consistent with Commission precedent, disallow Company adjustments for inflation, growth projections, forecasts and estimates;
5. Disallow recovery of $15,428,000 in bonuses;
6. Disallow recovery of $469,894,472 in incremental costs associated with the incremental increase in coal ash remediation and disposal costs related to North Carolina's Coal Ash Management Act ("CAMA"), on system-wide basis to be allocated proportionately to South Carolina;
7. Disallow DEC to earn a return on pre-construction costs associated with the cancelled Lee Nuclear Project;
8. Disallow recovery of a reserve for an End of Life Nuclear Fund;
9. Reject DEC's proposed amortization periods of three (3) years for Carolinas West Control Center, Lee Combined Cycle, and South Carolina Advanced Metering Infrastructure and adopt ORS's respectively recommended thirty (30), thirty-nine (39), and fifteen (15) year amortization periods;
10. Disallow recovery of $575,000 in legal fees associated with coal ash litigation; and
11. Allow $1,339,000 in rate case expenses which limits the Company's recovery of rate case expenses to those expenses that were sufficiently supported with documentation

[1] *See* Letter filed by DEC on March 20, 2019 re: ORS's proposed BFC.

(disallowance of $512,000), those expenses that do not contain estimates or forecasts (disallow $2,000,000) and exclude from rate base the unamortized balance of rate case expenses; and

12. Approve a 9.3% Return on Equity ("ROE").

## III. LEGAL ARGUMENTS SUMMARY

### 1. Notice Limitations on DEC's Commodity Charge

In its Application, DEC stated that if its Petition was granted, that the average customer using 1,000 kilowatt-hours ("kWh") of electricity each month would see an increase in their monthly bill of approximately $15.57. It also stated that it was requesting "an increase in the Residential BFC from $8.29 to $28.00 per month effective June 1, 2019". Application, P. 5, Para. 9.

The Notice of Filing and Hearing[2] sent to customers sets forth these numbers in detail:

> Duke Energy Carolinas requests that the proposed increases be effective on June 1, 2019. A typical residential customer using 1,000 kWh will see an increase of approximately $15.57 per month beginning with the rate effective date in this case, requested to be June 1, 2019, and then an increase of $1.54 per month beginning June 1, 2020 and an additional $1.92 per month beginning June 1, 2021, to incorporate costs for grid investments per the Grid Improvement Plan described in the Application. Page 19 of the Application describes the Grid Improvement Plan, which can be described, in part, as a long-term initiative built upon strategic, data-driven investments to improve reliability to avoid outages and speed restoration; harden the grid to protect against cyber and physical threats; and to expand solar and other innovative technologies across a two-way, smart-thinking grid. The Company proposes an increase in the Residential Basic Facilities Charge from $8.29 to $28.00 per month effective June 1, 2019. A copy of the Company's Application, *as well as the proposed rates, charges and tariffs* may be obtained from the Commission at the following address: Public Service Commission of South Carolina, Clerk's Office, 101 Executive Center Drive, Suite 100, Columbia, South Carolina 29210. Additionally, the Application is available on the Commission's website at

[2] *See* Revised Notice of Filing and Hearing and Prefile Deadlines in Docket No. 2018-319-E dated November 28, 2018.

> www.psc.sc.gov and is available from Heather Shirley Smith, Deputy General counsel, Duke Energy Carolinas, LLC, 40 W. Broad Street, Suite 690, Greenville, South Carolina 29601; or Frank R. Ellerbe, III, Esquire, Robinson Gray Stepp & Laffitte, P.C., Post Office Box 11449, Columbia, South Carolina 29211 (emphasis added).

On January 31, 2019, DEC filed an Affidavit with the Commission certifying that it had served the Notice of Filing and Hearing containing the above quoted language by either electronic or U.S. Mail on its customers.

On March 20, 2019, DEC filed a letter with the Commission stating that it agreed to accept ORS witness Michael Seaman-Huynh's recommended BFC of $11.96 for residential non-TOU customers, $13.09 for residential TOU, and $11.70 for SGS customers. Hrg. Ex. 31 and See, Tr. p. 1645, l. 14 - p. 1652, l. 25 and Tr. p. 1562, l. 19 - 24. The Company thus voluntarily withdrew the specific BFC requested in its Application. In reply to the Company's letter, ORS filed a response with the Commission on March 21, 2019 in which ORS clarified the $11.96 BFC in Mr. Seaman-Huynh's testimony was based on applying his proposed rate design methodology which, when applied to ORS's recommended adjustments, produces the BFC rates contained in DEC's letter. Hrg. Ex. 31. ORS's response further stated that ORS was not proposing a specific BFC rate be approved by the Commission, but the application of the proposed rate design methodology of ORS.

Finally, and most significantly, ORS advised the Commission that "to the extent the remaining revenue requirement is allocated to variable/volumetric component of rates, the increase could be higher than the variable/volumetric rates DEC noticed in its Application. Rates noticed by DEC must not violate the due process rights of its customers and must not result in a taking of property without sufficient notice." As testified by ORS witness Steven Hamm, until the Commission issues the final ruling in this proceeding, it cannot be known with certainty whether there is a problem with the sufficiency of the Notice provided to customers regarding the

Company's proposed volumetric charge. Tr. p. 1650, l. 20 - p. 1656, l. 8. As addressed by Mr. Hamm, notice has the potential to become an issue which ORS or some other party to this case may raise should the Commission's Order exceed the noticed volumetric charge. *Id. See,* S.C. Atty. Gen. Opinion, Sept, 26, 2017, p. 14 (addressing the Constitutionality of the BLRA), citing *Miss. Power Co. v. Miss. Pub. Service Comm.*, 168 So.3d 905, 916 (Miss. 2015).

As a result, both the Company and the Commission were notified of the potential Notice issue related to the Company's per kWh charge contained in its Application. The above facts support a finding by this Commission that the Company is entitled to no more than the noticed or current per kWh charge.

As to the initial request of the Company for an increase in the BFC from $8.29 to $28.00 for its non-TOU customers, ORS opposed the increase in BFC of 238% because it contradicts the long-accepted practice of gradualism in rate design. Tr. p. 2018-10, ll. 12-19.

ORS supports a lower BFC to limit the severe economic impact that such a high BFC would have on fixed and low-income customers. *State of Missouri ex re. Southwest Bell Telephone Co. v. Public Service Commission of Missouri*, 262 U.S. 276, 290, 43 S.Ct. 544, 547, ft. nt. 2 (1923) ("rates may in no event be prohibitive, exorbitant, or unduly burdensome to the public.") If an increase as proposed by DEC were approved, it would limit the customer's ability to effectively reduce their monthly bills by reducing the amount of electricity used. Gradualism is the progressive change of rates over time in a manner that mitigates rate shock to customers. A rise in rates of 238% is clearly counter to this basic ratemaking principle. See, Hrg. Ex. 42, Pirro Ex. 6. ORS additionally believes that such a large BFC sends improper and confusing price signals to customers. As noted in the ORS letter of March 21, 2019, ORS recommends that the Commission only allow DEC to increase BFCs to recover no more than 25% of any Commission approved

revenue increase assigned to each rate class. ORS believes that the proposed method of recovering its increased revenue requirement solely through the BFC violates that "the statutory standard of 'just and reasonable' rates. *See, Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 602, 64 S.Ct. 281, 287 (1944).

**2. Treatment of Accounting Deferrals and Adjustments**

**A. Removal of Certain Expenses for Bonuses, Awards, And Miscellaneous Items**

ORS proposed Adjustment #36 to remove Operation and Maintenance ("O&M") expenses that were not necessary for rate making purposes. Some such items include expenses related to sponsorship, lobbying, service awards, advertising and other miscellaneous items. Tr. p. 1602-16, ll. 14-17.

Subsequent to filing the Application, DEC proposed to remove $277,000 in expenses related to lobbying and image building advertising. Tr. p. 1602-16, ll. 18-19. ORS witness Smith proposed to remove $2,399,000 of O&M expenses related to the lineman's rodeo, spot bonuses, service awards, chamber of commerce membership dues and other miscellaneous items that were not necessary for the provision of electric utility services. Tr. p. 1602-16, ll. 14-17. During the three separate night hearings held in this Docket, this Commission heard from over 100 people who spoke in opposition to DEC's request to increase rates. A common theme heard throughout these hearings was how difficult it can be for customers to pay their electric bills while also putting food on the table and taking care of medical expenses. It is unacceptable to charge customers for such items like team meals, coffee, parties, flowers, and non-professional organization memberships when these expenses are not necessary to providing electric utility service. While DEC may not consider these extra expenses to be "luxury items,"[3] based on the testimony

[3] *See* Tr. p. 1962, ll. 14-20.

presented by customers at the night hearings in Spartanburg, Anderson, and Greenville, many of DEC's customers feel differently as they struggle to keep up with the rising costs of electricity. The Commission's position on these types of expenses is clearly stated in Order Nos. 91-595, 94-1229, 01-887, and 02-285. ORS's recommendation to remove expenses not related to the provision of safe and reliable electric service supports the Commissions Orders and ORS believes it is more appropriate for DEC's shareholders to bear the burden of these types of expenses.

**B. Recovery of Accounting Deferrals**

At issue in this case are the Company's request to recover costs from six ("6") different accounting orders ("deferrals") which the Company accumulated since the last general rate case. The Company proposes the recovery of these deferrals through Adjustments #7 for the Carolinas West Control Center, #13 for Lee Combined Cycle, #18 for Deferred Environmental Costs, #19 for SC AMI, #30 for Customer Connect, and #35 for SC Grid Mod. *See* Application, Ex. B. ORS reviewed each of the Company's proposals for recovery of accounting deferrals and developed a recommendation to be applied to the requests by the Company to recover its deferred costs. In each of the Company's proposed deferrals the Company calculated a weighted average cost of capital ("WACC") return on deferred costs. Additionally, the Company proposed to include the unamortized balance of each deferral in rate base. ORS recommended each deferral balance be separated into two categories of costs, operating-related costs and the capital-related costs. Tr. p. 1614, ll. 9-12. ORS recommended the recovery of both the operating-related costs and the capital-related costs be subject to the same regulatory accounting treatment required for each category absent an accounting deferral. Tr. p. 1614, ll. 12-16. Additionally, ORS recommended a change to the amortization period for the deferrals in Adjustments #7, 13, 19, and 35, to equate the amortization periods of the deferrals to the lives of the underlying assets for which costs are being

deferred. Lastly, ORS witness Wittliff recommended that the Commission disallow $469,894,472 of the $876,206,294 in total system Asset Retirement Obligation ("ARO") deferrals being requested by the Company in this proceeding, which relate to the Deferred Environmental Costs in Adjustment #18. ORS's recommendation for this adjustment is addressed in detail in ORS witness Wittliff's Direct and Surrebuttal Testimonies and a separate section of this brief.

By way of background, an accounting order to defer costs (commonly known as a deferral) is a regulatory instrument that occurs when this Commission approved a utility's request to establish a regulatory asset (or liability) account into which certain costs can be deferred. The Financial Accounting Standards Board's ("FASB") ASC 980 provides general standards of accounting addressing the effects of regulation, and ASC 980-340-25-1 specifically states that:

> A regulated business-type activity should capitalize all or part of an incurred cost that otherwise would be charged to expense if both of the following criteria are met:
>
> a. It is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes.
> b. Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs.

While FASB outlines the accounting standards for deferring costs, it is ultimately this Commission which must determine what costs in the regulatory asset are allowable for ratemaking purposes, and the way by which the utility is permitted to recover those allowable costs in the regulatory asset. While ORS is not contesting the prudency of the dollar amount of expenses, with the exception of costs related to coal ash remediation and disposal, it does object to the Company being allowed to collect a return from its customers on deferred operating expenses and urges the Commission to deny the Company the ability to do so.

ORS recommends the Commission allow recovery for the expenses in the deferral account in the same manner that the expenses would be recovered absent the deferral account. First, the

Company's deferred expenses must be separated into two categories: 1) operating-related costs, and 2) capital related costs. Both categories should then be subject to the same regulatory accounting treatment which would be applied absent an accounting deferral. With the exception of certain coal ash management and disposal costs, ORS does not claim any of the dollars in the deferral accounts were imprudently incurred or otherwise non-allowable.

ORS disputes the Company's assertion that it is entitled to earn a weighted average cost of capital ("WACC") return on its deferred operating-related or O&M expenses. ORS maintains that it is improper and counter to sound ratemaking principles to allow the Company to charge its customers a return on deferred O&M expenses as these same expenses which, if not deferred, would not be permitted to generate a return for the utility. DEC witness Smith mischaracterizes the ORS position by stating "[t]he ORS makes several recommendations with regards to deferred costs which would in effect deny the Company recovery of prudently incurred costs." Tr. p. 659-5, ll. 6-8.

In short, O&M expenses are not entitled to a WACC return and are not appropriate to include in rate base. However, the Company may recover prudently incurred and deferred capital costs by recording capital costs to rate base and recovering those costs through amortization expense over the life of the asset, while earning a WACC return on the unamortized balance.

This Commission has issued four (4) orders approving the deferrals the Company is requesting to recover in this docket. Order 2016-489 approved the SC AMI deferral; Order 2016-490 approved the Coal Ash deferral; Order 2018-552 approved three (3) deferrals: Carolinas West Control Center, Lee Combined Cycle, and Customer Connect; and Order 2018-751 approved the GridMod deferral. While these Commission orders approved the Company's request to defer the expenses detailed in their petitions, they do not provide any guarantee to the Company to recover

these deferred expenses. In fact, each Commission order contains language stating that the issuance of an order approving the deferral will not prejudice any party from addressing the prudency and reasonableness of the deferrals in the Company's next rate case proceeding.

The dollar amounts at issue here are significant. ORS's recommendations allow the Company to include costs that were largely incurred outside of the test year ending December 31, 2017 ("Test Year"), by including approximately $24,000,000 in amortization expense and including approximately $115,000,000 in unamortized deferral balances in rate base. ORS's recommended accounting treatment contributes approximately $33,000,000 to the ORS proposed revenue increase of $82,357,000 or more than 40%. In comparison, the Company's proposals related to recovery of deferred balances included approximately $75,000,000 in amortization expense and approximately $243,000,000 in unamortized deferral balances in rate base. The Company's recommended treatment contributes roughly $94,000,000 (more than 40%) to the Company proposed revenue increase of $230,807,000.

In support of its position that DEC is entitled to returns on deferred operational expenses removed by ORS, the Company presented Rebuttal testimony from its witnesses Smith, Wright, and Hevert. Those Company witnesses alleged great financial misfortune if the Company was not allowed to collect a return on these deferred operational expenses. However, in each case, the Company's witness failed to acknowledge that the Company had collected $1.7 billion dollars in operating revenues from South Carolina customers during 2017 through rates that were designed to allow recovery of the Company's operating costs as well as provide a reasonable return on shareholders' capital investments. Therefore, the Company does not, as implied by its witnesses, rely solely on investments from equity holders or funds raised through the issuance of debt to generate cash to support its operations. The Company did not offer an accounting principle or

relevant case law to support its claim of entitlement to a return on deferred operational expenses. Unlike the Company's position, ORS's recommendation achieves an equitable sharing of deferred costs between the Company's customers and the Company's shareholders. "[T]he fixing of 'just and reasonable' rates involves a balancing of the investor and the consumer interests. *Fed. Power Comm'n v. Hope Natural Gas, Co.,* 320 S.C. 591, 603, 64 S.Ct. 281, 288 (1944).

ORS's proposals represent a reasonable, equitable, and lawful approach to allowing the Company's recovery of deferred costs. ORS's recommendations would allow the Company to include and recover certain costs that were primarily incurred outside of the Test Year, by including approximately $24,000,000 in amortization expense and including approximately $115,000,000 in unamortized deferral balances in rate base. As illustrated in Table 1.1 at page 3 of Mr. Payne's Surrebuttal Testimony, the ORS's recommended accounting treatment equates to approximately $33,000,000, or 40%, of the ORS proposed revenue increase of $82,357,000. Tr. p. 1617-3, l. 1.

**C. <u>Adjustments for Growth Projections, Inflation and Contingencies</u>**

ORS opposed certain adjustments proposed by DEC that accounted for growth projections, inflation and contingencies which the Company included in its Application. ORS witness Gaby Smith included in her audit adjustments recommendations that the Commission deny the Company the right to recover from customers certain estimated adders for "growth projections" and "inflation" to its Adjustment #20 for Storm Costs, Adjustment #21 for Non-Labor O&M, Adjustment #28 for Credit Card Fees and a portion of Adjustment #30 to normalize O&M for Customer Connect expenses. This position is based on the longstanding accounting principle that any adjustments to Test Year expenses must be both known and measurable. See, Tr. p. 1602-14, ll. 4-9. *Heater of Seabrook, Inc., v. Public Serv. Comm'n of S.C.*, 324 S.C. 56, 60, 478 S.E. 2d

826, 828 (1996). As the inflation and growth projections proposed by the Company are neither known nor measurable for regulatory principles, but merely estimates formulated by DEC employees, they should be denied by the Commission. See, Tr. p. 1010, l. 9 – p. 1012, l. 23.

As part of Adjustment #30, the Company proposed to adjust other O&M expenses by $4,025,000 to increase its test year O&M expense from $640,000 to recover projected and estimated costs totaling approximately $4,665,000, related to the development of its new customer billing interface known as Customer Connect. DEC witness Hunsicker provided a breakdown of the Company's estimated expenses in her Rebuttal Testimony, which included a $1,800,000 category she described as "[t]o ensure forecasted costs to cover inflation and contingency. Tr. p. 980-6, ll. 8-15. DEC witness Smith requested through her Rebuttal Testimony that "[a]t a minimum, the Company's actual O&M in 2018 of $3,189,000 should be allowed." Tr. p. 659-18, ll. 20-21. Through Surrebuttal Testimony, ORS witness Smith updated ORS's position on Customer Connect O&M expense to accept the 2018 actual O&M amount recommended by DEC witness Smith, resulting in an adjustment of $2,549,000. Tr. p. 1607-8, ll. 16-22. Regarding DEC's expenses for its Customer Connect program, ORS recommends this Commission accept the Company's and ORS's request for an adjustment to O&M of $2,549,000 to permit the Company to recover its actual 2018 O&M expenses of $3,189,000. Per S.C. Code Ann. Regs.103-823(A)(3), it is undisputed that rate applications must be based on a historic 12-month test period. Traditionally, the Commission allows adjustments to the Test Year to reflect known and measurable changes in the Company's operating experience. By adjusting the Company's Test Year to the 2018 actual expense amount represents a known and measurable change to the Company's Test Year. The Company's initial recommendation to recover approximately $4,700,000 million dollars would permit the Company to recover costs that are based on

contingency and inflation. Adjustments for inflation and "contingencies" are not known and measurable. Therefore, consistent with Commission Order Nos. 84-108 and 85-841, in which the Commission expressly rejected adjustments for inflation, ORS recommends the Commission continue to reject recovery of these costs, which are simply based on projections and estimates, and serve to shift the risks from the Company to the customers *See Id.* Due to ORS's adjusting for the Customer Connect expense level experienced by the Company for calendar year 2018, ORS recommends cancellation of the accounting order (Order No. 2018-552) for deferred expenses related to Customer Connect on the date of the order issued by the Commission in this docket.

ORS opposes both inflation-based estimates as well as the 20% growth projections included by the Company in its calculation of credit card fees. Per S.C. Code Ann. Regs.103-823(A)(3), the Commission requires that rate applications be based on a historic twelve-month test period. Traditionally, the Commission allows adjustments to the test year to reflect known and measurable changes in the Company's operating experience. In explaining ORS Adjustment #28 ORS witness Smith asserted the ORS position that adjustments for growth projections are not known and measurable. This is consistent with Commission Order Nos. 84-108 and 85-841. Tr. p. 1607-14, ll. 4-9. ORS recommends the Commission again reject recovery of these projected and estimated costs as they are only based on projections and estimates which unfairly shift certain risks from the Company and its shareholders to the customer.

While Company witness Quick stressed in her rebuttal testimony how much customers like the ability to pay by credit card with no fee, the only support for the inclusion of additional dollars for a growth projection is a general claim that the Company expects more customers to use this payment option and thus the Company anticipates having increased costs. Tr. p. 984-4, l.13 - p. 984-6, l. 2. Notably, the Company is offering estimates of increased costs but was unable to offer

any information on increased cost savings. Tr. p. 735, ll. 17-20. Allowing estimates of future expenses is counter to established accounting principles which provide that any out-of-test year expenses must be known and measurable. "When calculating expenses in rate cases, Commission should use only test year data and known and measurable changes occurring after the test year." *Heater of Seabrook, Inc. v. Public Serv. Comm'n of South Carolina,* 324, S.C. 56, 60, 478 S.E. 2nd 826, 828 (1996) citing *Southern Bell Tel & Tel. Co. v. South Carolina Pub. Serv. Comm'n*, 270 S.C. 590, 244 S.E.2d 278 (1978). Notably, the Company failed to balance these projected costs against any projected savings that may be generated by an increase in DEC customers timely payments using credit cards.

As established in *Accounting for Public Utilities*, there are only five (5) recognized categories of pro forma adjustments to a Test Year. Those are: 1) normalizing adjustments, 2) annualizing adjustments, 3) our-of-period adjustments, 4) attritional adjustments, and 5) reclassified items. *Accounting for Public Utilities*, §7.05, pg. 7-6, Pub. 16, Rel. 35 (Nov. 2018). None of the above estimated expenses proposed by the Company meet any of these exceptions. Further, there is no statute, regulation, or accounting principle that permits the Company to collect from customers such unknown and speculative expenses. The DEC proposal is essentially prospective or alternative rate making, which is not the rate making methodology adopted by the South Carolina General Assembly and implemented this Commission. The use of a historical test year has been reviewed and approved by the South Carolina Supreme Court "as a basis for calculating a utility's rate base as long as adjustments are made for any *known and measurable* out-of-period changes in expenses, revenues, and investments that would materially alter the rate base." *Porter v. South Carolina PSC,* 328 S.C. 222, 228, 493 S.E.2d 92, 96 (1997) (emphasis added).

In its Application, DEC seeks to add an inflation adjustment to calculate its 10-year average storm expense adjustment amount, claiming the inflation adjustment is warranted to mitigate the impact of regulatory lag. Tr. p. 651, ll. 1-6. The Company also requested an adjustment to annualize Test Year O&M non-labor expenses for inflation to reflect the change in costs that occurred during the test period. Tr. p. 659, ll. 11-12. ORS recommends this Commission reject the addition of adjustments for inflation as they are not known and measurable. Tr. p. 2013, ll. 12-17. This Commission has previously expressly rejected adjustments for inflation in Order Nos. 84-801 and 85-841, stating an inflation rate applied prospectively is "generalized and speculative and accordingly should be rejected."[4] ORS's adjustment to normalize for storm costs does not include an amount for inflation and ORS does not propose an adjustment to normalize O&M non-labor expenses for inflation. Tr. p. 1602-11, ll. 18-19.

**D. Bonus Pay**

ORS recommends the costs of bonuses, DEC's Long Term Incentive ("LTI") and Short-Term Incentive ("STI") plans, be shared equally between customers and shareholders. Tr. p. 1607-5, ll. 10-11. ORS witness Smith testified this Commission should disallow 50% of the Company's LTI and STI program costs, resulting in a total disallowance of $15,428,000. Tr. p. 1602-12, ll. 6-9.

DEC witness Metzler testified incentive pay is linked to specific goal accomplishments and the purpose is to encourage employees to accomplish certain objectives, to ensure DEC's overall success, and to incorporate a component of any compensation package that is competitive based on the market. Tr. 1139-5, ll. 7-15. All employees have STI as a component of their total pay and is variable based on performance and is at risk to the employees. Tr. 1139-5, ll. 5-7. LTI

[4] See Docket No. 1985-78-E, Order No. 85-841, p. 22.

plans are compensation components of certain identified employees in leadership positions. Tr. 1139-5, ll. 15-17. A portion of DEC's STI and LTI plans consist of Earnings Per Share ("EPS") and Total Shareholder Returns ("TSR"), which are based on the market performance of the Company's stock. Tr. p. 1139-10, l. 21- p. 1140, l. 9. DEC's Executive Leadership Team's[5] ("ELT") STI payouts are based on 50 % EPS and all non-ELT employees' STI payouts are based on 30 % EPS. Tr. p. 1139-11, ll. 1-3. DEC's ELT's LTI plans are based 50 % on EPS and 25 % on TSR for a total 75% of the LTI payouts directly tied to DEC's stock performance. Tr. p. 1141, ll. 19-23. DEC witness Metzler testified the EPS and TSR measure how much money the Company is making for its shareholders. Tr. p. 1141, l. 24 – p. 1142, l. 4. DEC also has a group of about 550 employees who are eligible for the LTI plan that consist of retention awards only, not performance based. Tr. p. 1156, 11. 15-25.

ORS witness Smith testified an adjustment of 50 % of the LTI and STI program costs would equitably share the costs between customers and shareholders. Tr. p. 1607-5, ll. 10-11. Due to the fact that these incentives are largely tied to stock performance rather than service to customers, a balanced approach fairly reduces the total burden being placed on customers. Tr. p. 1607-4, ll. 7-12. ORS witness Smith testified an increase in DEC's EPS and TSR due to an increase in rates substantially influences the LTI and STI payouts made to employees and removes the incentive to achieve earnings goals through performance, customer satisfaction, efficiencies, and cost reduction measures. Tr. p. 1607-4, ll. 13-17. DEC's shareholders are the primary benefactors of increased EPS and TSR, which the LTI and STI are largely based upon. Tr. p. 1607-4, ll. 17-18. This Commission has previously found that "[i]t is just, reasonable, and consistent

[5] DEC's ELT consists of about 100 employees, including senior management. Tr. p. 1161, ll. 6-7.

with sound regulatory policy to allow [a utility] to recover one-half of the cost of incentive pay for its officers and employees through rates."[6]

### 3. Incremental Costs Related to Coal Ash Basin Closure

DEC is seeking recovery of Coal Combustion Residuals ("CCR") expenses incurred from January 2015 through December 2018 related to compliance with Federal and State regulatory requirements. ORS does not oppose DEC's request to recover expenses incurred related to compliance with the Federal CCR rule. However, as part of its request, DEC seeks recovery of approximately $469,894,472 which constitutes additional expenses incurred strictly due to the requirements imposed by the North Carolina General Assembly on coal ash basins located in North Carolina. Tr. p. 1340-9, ll. 13-16. North Carolina enacted the CAMA in 2014, partly in response to the massive coal ash spill into the Dan River caused by a drain pipe failure at DEC's retired coal-fired plant in Eden, North Carolina. Tr. p. 1340-17, l. 5 – p. 1340-18, l. 41. Both the Federal CCR rule and CAMA dictate how coal ash basin closure is to be handled, however the CAMA requirements are both stricter and costlier than the Federal CCR rule. Tr. p. 1340-21, ll. 1-4. As stated by DEC witness Smith, the costs to comply with CAMA and the Federal CCR rule are somewhat duplicative but there is a portion of the costs that "the Company has determined are specific to CAMA, unique to North Carolina and appropriate for direct assignment to North Carolina." Tr. p. 655-22, ll. 13-17. ORS agrees with DEC witness Smith, costs incurred related to CAMA are unique to North Carolina and should be directly assigned to North Carolina customers. Requiring South Carolina customers to pay for costs incurred due to legislation adopted in another state is the definition of "taxation without representation."

[6] See Docket No. 2012-218-E, Order No. 2012-951, p. 18.

DEC has eight (8) coal-fired generating facilities with ash basins. Coal-powered electric generation stations are no longer in use at four (4) of those eight: Dan River, Buck, Riverbend, and W.S. Lee. Tr. p. 1232-11, ll. 17-19. The W.S. Lee facility is DEC's only coal-fired generating facility in South Carolina. In September 2014 DEC entered into Consent Agreement 14-13-HW ("Consent Agreement") with the South Carolina Department of Health and Environmental Control ("DHEC"). Tr. p. 1232-17, ll. 17-19. This Consent Agreement differed from the Federal CCR rule in that in addition to requiring DEC excavate ash from the plant's Primary and Secondary ash basins it also required DEC to excavate the Inactive Ash Basin and the Ash Fill Area. Tr. p. 1232-17 l. 19 – p. 1232-18, l. 2. DEC conducted coal ash cleanup at its North Carolina facilities as dictated by State and Federal regulations. DEC witness Kerin testified the Company is closing its ash basins in accordance with the most restrictive requirements contained in CAMA. Tr. p. 1232-8, ll. 10-12. For the basins located in North Carolina, the Federal CCR rule required action at all of DEC's facilities except Riverbend, as the Federal CCR Rule does not currently apply to inactive impoundments. Hrg. Ex. 29, Kerin Ex. 5. For the basin closures at the other six DEC North Carolina facilities, the Federal CCR Rule required either excavation or cap-in-place. Tr. p. 1232-26, ll. 3-7. Unlike the Federal CCR Rule, CAMA required closure of all basins in North Carolina. Hrg. Ex. 33 at DJW-8.1.2. Under CAMA, the basins are all ranked by risk to the public and the environment from low to high priority. Tr. p. 1232-29, ll. 3-5. The level of risk as determined by CAMA dictates the closure method. Tr. p. 1388, ll. 14-24. DEC's Allen, Belews, Cliffside, and Marshall facilities were deemed intermediate risk by CAMA, but DEC was able to reduce the level of risk by ensuring dam safety and replacing water supplies to neighboring residents. Hrg. Ex. 29, Kerin Direct Ex. 9. By reducing the level of risk to low priority, DEC will be able to utilize cap-in-place as mandated by the Federal CCR Rule at these facilities. *Id.* The Buck facility was deemed

intermediate priority and DEC opted to conduct onsite beneficiation at this facility. *Id.* CAMA required DEC to utilize beneficiation at three (3) facilities of DEC's choosing. Tr. p. 1268, ll. 9-11. The Dan River facility was deemed high priority according to CAMA and had to be excavated. Hrg. Ex. 29, Kerin Direct Ex. 9. The Riverbend facility, though exempt from the Federal CCR rule, was deemed high priority under CAMA and therefore had to be excavated. Hrg. Ex. 29, Kerin Direct Ex. 9.

If CAMA were not in place beneficiation at the Buck facility would not have been required. ORS witness Wittliff testified that the closure of the Buck site resulted in additional costs of $36,544,788 on a system-wide basis that was solely the result of the beneficiation requirement under CAMA. Tr. p. 1340-35, l. 2 – p. 1340-36, l. 2.

If CAMA were not in place DEC would have had additional time to close the Dan River site. Tr. p. 1340-26, l. 7-23. ORS witness Wittliff testified that CAMA accelerated the closure timeline at the Dan River facility which resulted in $116,669,019 of additional costs on a system wide basis that was solely the result of CAMA. Hrg. Ex. 33 at DJW-8.1.2.

If CAMA were not in place, basin closure at the Riverbend facility would not have been required. ORS witness Wittliff testified that the closure at Riverbend was solely the result of CAMA requirements and that there was no requirement to close the facility under the Federal CCR Rules, this should result in a disallowance of $316,680,655 on a system-wide basis. *Id.*

As explained by ORS witness Seaman-Huynh, DEC utilized a cost causation allocation method on certain costs the Company directly assigned to its North Carolina and South Carolina jurisdictions, respectively. Tr. p. 2028-5, ll. 20-21. Cost causation allocation puts the cost responsibility for expenses and rate base items on the customer class that caused the expenses to be incurred. Tr. p. 2028-3, ll. 15-20. DEC directly assigned expenses incurred due to South

Carolina's Distributed Energy Resource Program ("DERP") Act to South Carolina customers and directly assigned expenses incurred due to the North Carolina Renewable Energy and Energy Efficiency Portfolio Standard and the North Carolina Clean Smokestacks Act to North Carolina customers. Tr. p. 2028-6 l. 21 – p. 2028-7, l. 1. ORS witness Seaman-Huynh testified it is a common practice for utilities operating in multiple jurisdictions to assign the costs related to certain accounts directly to one jurisdiction as these costs are often derived from laws and regulations that are specific to that jurisdiction. Tr. p. 2028-7, ll. 1-3.

DEC witness Kerin testified the Company is not seeking recovery of costs incurred to supply clean drinking water to North Carolina residents affected by the Dan River coal ash spill as that expense is "unusual" and "unique." Tr. p. 1279, ll. 9-14. CAMA's requirements are also unique – unique to the state of North Carolina, and the burden of its required expenses should not fall on South Carolina customers. ORS recommends this Commission protect South Carolina customers from an increase in rates due to the incremental increases in costs imposed by CAMA above the Federal requirements. CAMA includes protections above and beyond what is required in the Federal CCR Rule and these protections are only to the benefit of North Carolina residents.

**4. Return on Pre-Construction Costs Associated with the cancelled Lee Nuclear Project**

In its Application, DEC requested recovery of pre-construction costs for the cancelled Lee Nuclear Project. ("Lee Nuclear") App. p. 10, para. 17. ORS recommends this Commission disallow a return on debt or equity for these costs. ORS witness Morgan testified earning a return on these costs is not supported by the manner in which DEC made its request. Tr. p. 2017-4, ll. 16-18. DEC witness Smith testified disallowing a return on the costs associated with Lee Nuclear would be punitive and arbitrary, as South Carolina Electric and Gas Company "(SCE&G") is

recovering costs for the failed V.C. Summer project with a return. Tr. p. 659-12, ll. 11-14. However, as ORS witness Morgan testified, SCE&G filed under the Base Load Review Act ("BLRA") which allowed SCE&G to earn a return on the pre-construction costs related to the failed V.C. Summer project. Tr. p. 2017-4, ll. 11-15. DEC made its request in a general rate case and due to the status of Lee Nuclear, it does not belong in rate base and is not entitled to a return. Tr. p. 2017-4, ll. 16-22. Lee Nuclear does not meet the criteria to be placed in "plant in service" nor can it be categorized as "property held for future use" or "construction work in progress." Id.

This Commission has previously held that it is not reasonable to require customers to pay a return on an investment that is not used and useful, stating "[t]he inclusion of the unamortized balances in rate base would be inconsistent with the ratemaking principle that the Company is entitled to earn a return on the investment used and useful in providing service to the ratepayers."[7] ORS witness Morgan testified the Customers should not have to pay a return on a cancelled project when they have not and will not receive any benefit from that project. Tr. p. 2017-5, ll. 3-4. ORS recommends the risks of the cancelled Lee Nuclear Project be equitably shared between the DEC shareholders and its customers through the disallowance of a return on debt and equity.

**5. <u>The Establishment of a Reserve for End of Life Nuclear Costs</u>**

In its Application, DEC has sought to recover $6.975 million every year from DEC customers to be placed into a "reserve" fund until its nuclear plants are decommissioned. This significant pot of money, to be collected from customers for an infinite period, would be used by DEC to pay for estimated end of life nuclear fuel and parts inventory. Neither the decommissioning dates, cost of fuel, or inventory of parts are known or measurable. As with the Company's requests for inflation and contingency adjustments, DEC is asking that the

[7] *See* Order No. 1983-92, Docket. No. 1982-50-E.

Commission detour from the well-established standards used in historical test year rate cases. *See, Heater of Seabrook, Inc., supra.*

As testified to by ORS witness Morgan and DEC witness Capps, DEC's operating licenses for the Company's nuclear units are currently set to expire between 2033 and 2043. See, Tr. p. 2015-4, ll. 13-15. This means that the earliest the Company anticipates that it **may** need additional decommissioning costs is between fourteen (14) and twenty-four (24) years from now. Yet those dates may have no relationship to the dates when these nuclear facilities are decommissioned.

[redacted] "When calculating expenses in rate cases, Commission should use only test year data and known and measurable changes occurring after the test year." *Heater of Seabrook, Inc. v. Public Serv. Comm'n of South Carolina*, 324 S.C. 56, 60, 478 S.E.2d 826, 828 (1996).

Not only are these costs not known or measurable, but it is irrational to ask customers to pay for funding a bucket full of money for DEC to maintain for over thirty (30) years, when the Commission has directly heard from numerous customers that they cannot pay their DEC bills now. See, Tr. Volumes 1 -3 (Public Night Hearings held in Spartanburg, Anderson, and Greenville) and Hrg. Ex. 58 (confidential). ORS's recommended adjustment to remove these end-of-life nuclear reserve fund costs are shown on Hrg. Ex. 43 at GS-2, Adjustment #15. Although DEC witness Capps claims that "it is in the best interest of today's customers" for the Company to start collecting almost $7 million each year in additional revenues from them, it is difficult to see how this statement could be true. Tr. p. 911-3, ll. 18-19.

### 6. Appropriate Amortization Periods

In its Application, DEC proposed three-year amortization periods for deferred cost balances related to the Carolinas West Control Center, the W.S. Lee Combined Cycle Facility, and the South Carolina Advanced Metering Infrastructure ("AMI"). ORS witness Morgan testified it is reasonable to base the amortization period upon the life of the underlying asset as that is the period in which it is anticipated to benefit the customer who is paying for the asset. Tr. p. 2017-2, ll. 17-19. ORS recommends this Commission set the amortization period for the Carolina West Control Center at thirty (30) years, the W.S. Lee Combined Cycle Facility at thirty-nine (39) years, and fifteen (15) years for the South Carolina AMI. Tr. p. 2017-3, l. 1. ORS witness Morgan testified ORS's recommendations were consistent with the service life of the associated asset. Tr. p. 2017-2, ll. 19-20. DEC witness Smith testified amortization periods are subjective, but failed to provide rationale for the periods the Company proposed in its Application. Tr. p. 659-11, ll. 1-5. The adoption of ORS's recommended amortization periods will lessen the effect on the revenue requirement, and the impact on rates is nominal. Tr. p. 2017-3, ll. 2-3.

### 7. Insurance Litigation, Legal Fees, and Rate Case Expenses

ORS contests the recovery of two (2) categories of legal expenses, the first consisting of certain litigation expenses and legal fees related to coal ash and the second consisting of rate case expenses. ORS recommends this Commission limit recovery of these categories of legal expenses to only incurred costs that are supported by sufficient supporting documentation to show the legal expenses are approved regulatory expenses that are recoverable through rates.

#### A. Legal Fees and Litigation Expenses

ORS recommends this Commission deny the recovery of $575,000 in litigation expenses attributed to legal actions related to coal ash. Tr. p. 1604-2, ll. 13-15. According to the Company,

these legal expenses supposedly relate to the ongoing insurance recovery litigation and the defense of state enforcement actions. Tr. p. 1604-2, ll. 15-19. In response to ORS discovery requests, DEC provided limited information regarding the nature of the legal expenses making it difficult for ORS to verify and determine whether the expenses were the result of management decisions or whether the expenses resulted in an outcome economically beneficial to DEC's customers. Tr. p. 1607-5, l. 19 – p. 1607-7 l. 4.

The ongoing insurance litigation was initiated by DEC to obtain indemnity from insurers for costs incurred associated with coal ash remediation. Tr. p. 1247-26, ll. 7-10. DEC witness Wright testified DEC believes some of the coal ash remediation costs *may* be recoverable, but the insurance company has denied any payout to date. (Emphasis added.) Tr. p. 1310, ll. 1-21. DEC witness Kerin testified that the litigation is currently in the discovery phase and while there have been some settlement discussions there could be a trial sometime in 2020. The outcome has not been determined to date. Tr. p. 1311, l. 23 – p. 1312, l. 1. This Commission has held that legal expenses incurred where the utility was found at fault and was unable to demonstrate an outcome that provided an economic benefit to its customers will not be included in rates paid by customers, but should be the burden of stockholders instead.[8] With regard to these insurance litigation expenses, there is no specific information from DEC for the Commission to determine the benefit to customers or to approve recovery through rates. The litigation is pending, customers have not received any benefit, and it is unknown at this stage whether any benefit will occur. Should DEC lose in this litigation due to a finding that DEC is at fault and not entitled to insurance coverage, these litigation expenses should be assigned to stockholders as this Commission previously held

[8] Docket No. 2017-292-WS, Order No. 2018-802.

in Docket No. 2017-292-WS, "Application of Carolina Water Service, Incorporated for Approval of an Increase in Its Rates for Water and Sewer Services."

Much like the litigation expenses related to the ongoing insurance litigation, DEC has not provided enough information detailing the nature of other coal ash related legal fees incurred during DEC's defense against state enforcement actions. Despite three (3) separate requests, DEC failed to provide sufficient specific information necessary to support the recovery of legal expenses through customer rates. At the request of Commissioner Ervin in regard to $250,000 of legal expenses associated with coal ash litigation, DEC submitted Late Filed Hearing Exhibit 56 which purportedly provided matter descriptions and line item detail.[9] By submitting a late filed exhibit, ORS is denied the opportunity to fully vet and review the materials provided to the Commission and denies ORS its right of cross examination of the sponsor of the exhibit. ORS protested the introduction of this late filed exhibit into the record of this case.[10] DEC had multiple opportunities to provide the information requested by ORS, but repeatedly failed to do so and has continued to feign ignorance as to what information ORS requested. Tr. p. 1955, ll. 4-20. DEC witness Smith testified DEC would have provided more detailed information had ORS requested it, but claimed ORS only requested "paper invoices" which the Company does not have. Tr. p. 1955, ll. 4-7. DEC witness Smith testified DEC has the ability to review what they are billed by outside counsel in the electronic billing system, and that the same information is in this electronic billing system that one would typically find on a paper invoice. Tr. p. 1969, l. 11 – p. 1971, l. 4. However, when DEC exported this info into the excel spreadsheets they submitted to ORS and this Commission, the full scope of the information available does not export into the spreadsheet. When questioned

[9] *See* letter filed by DEC on April 1, 2019.
[10] Letter Responding to Late Filed Exhibit 56 https://dms.psc.sc.gov/Attachments/Matter/2b3a21e7-1d1f-4769-bcda-1db27c32e6ff.

by Commissioner Ervin, DEC witness Smith testified she had seen spreadsheets containing descriptions of services rendered but agreed that the one provided in response to ORS Audit Request 55-5 did not have that information. Tr. p. 1985, ll. 1-7. DEC witness Smith acknowledged the Company has the burden of proof, yet implied that ORS failed to submit the appropriate request in order to get the desired information. Tr. p. 1985, l. 14 – p. 1986, l. 4.

It must be noted that whether the Company uses paper invoices or not the burden of proof is on DEC to justify the request to recover expenses. *Hilton Head Plantation Utilities Inc. v. Public Service Com'n of SC*, 312 S.C. 450, 441 S.E. 2d 323, (1994). When payments are made to a third party, a "mere showing of actual payment does not establish a *prima facie* case of reasonableness." *Id.* As for Late Filed Hearing Exhibit 56, the spreadsheets provided still fail to show sufficient specific evidence to support for the recovery of the requested expenses. Based on the information provided by DEC, this Commission cannot determine if any listed fees, costs or expenses qualify as an approved regulatory expense for inclusion in DEC customer rates. There is no way to determine if the listed litigation against DEC is the result of adverse judicial decisions resulting from poor management operating conditions. The matter numbers provided are not self-explanatory and are essentially useless in a regulatory proceeding, therefore ORS asks this Commission to disallow $575,000 in unsupported litigation expenses and legal fees.

**B. Rate Case Expenses**

The Company proposes in its Application Adjustment #25 to amortize rate case expenses of approximately $3,852,000 over five (5) years or $770,000 annually. The total amount of rate case expenses proposed by the Company includes projected expenses of approximately $2,000,000 through May 2019. Of the remaining actual $1,851,000 in rate case expenses, the Company was unable to provide sufficient documentation in support of $512,000. ORS recommends this

Commission allow the Company to amortize a total of approximately $1,399,000 in rate case expenses over a five (5) year period, resulting in an annual amortization expense of $268,000 as recommended in Hearing Exhibit 44, GS-2. ORS recommends this Commission not allow the Company to recover $512,313 in rate case expenses due to lack of supporting documentation, or $2,000,000 for estimated expenses as they are not known and measurable.

On December 12, 2018, ORS sent an Audit Request to the Company requesting actual rate case expenses for this docket as they became available and requesting that the Company include "a summary listing of expenses, copies of all invoices and proof of payment." DEC responded with excel files related to rate case expenses. ORS repeatedly requested supporting documentation for the excel file titled "DEC Confidential Legal Invoices" the Company initially provided in order to review the expenses, but the Company failed to provide them. In Docket No. 2006-92-WS, this Commission held that it did not have enough evidence to be able to evaluate the reasonableness of attorney's fees, specifically, and rate case expenses in general. *In re Carolina Water Service, Inc.*, 2007 WL 4944726 (S.C.P.S.C.).[11] This Commission held that the complete lack of evidence on rate case expenses, other than the provision of the numbers themselves, severely limited the Commission's ability to make an independent determination as to the justifiable expenses. *Id.* Similar to *In re Carolina Water Service, Inc.*, without proper evidence here the Commission cannot properly evaluate the expenses claimed, there this Commission should disallow the recovery of $512,313 in unsupported rate case expenses. Also, ORS recommends this Commission disallow

[11] In Docket No. 2006-92-WS, the Commission ultimately approved the Settlement Agreement which contained the requested rate case expenses only after a subsequent hearing where Carolina Water Service provided the requisite information to justify the expenses. Here, DEC has been provided ample opportunities to provide ORS with the material and was even granted leave to submit a late filed exhibit, yet DEC has still failed to justify these expenses at issue here.

the inclusion of unamortized rate case expenses in rate base. Including unamortized rate case expenses in rate base would allow the Company to earn a return on operating expenses.

**8. Rate of Return and Cost of Capital**

Three (3) parties' witnesses addressed the issue of Return on Equity ("ROE" or "Cost of Equity"). Robert Hevert testified on behalf of DEC, David Parcell for ORS, and Gregory Tillman on behalf of Intervenor Wal-Mart.

The Company is, by law, entitled to a reasonable return on its allowable costs. See, *Federal Power Comm'n v. Hope Natural Gas Co.,* 320 U.S. 591, 64 S.Ct. 281 (1944) and *Bluefield Water Works and Improvement Co. v. Public Service Comm'n*, 262 U.S. 679, 43 S.Ct. 675 (1923). However, ORS does not believe that it is a reasonable or fair balancing of the interests of the Company and its customers to approve an inflated ROE that not only exceeds what has been found to be reasonable by other Commissions across the country over the past three (3) years, but would in fact be the highest ROE awarded to any electric utility in the United States. See, Hrg. Ex. 26, DCP-2, Schedule 3. While a public utility is entitled to earn a fair return, it has no entitlement or constitutional right to earn profits comparable with highly profitable enterprises or speculative ventures. *Bluefield v. Pub. Serv. Comm'n*, 262 U.S. 679, 690. ORS therefore urges that this Commission find that the analyses and methodologies used by Mr. Parcell is the most compelling of those presented into evidence in this case and either adopt his recommended ROE of 9.3% or accept the alternate proposal made by the ORS of 9.76%.[12]

DEC witness Hevert filed Direct and Rebuttal Testimonies providing his recommended ROE in this proceeding. Specifically, Mr. Hevert recommended a ROE for DEC of 10.75% within a range of 10.25% and 11.25%. In the Company's Application, DEC requested that the

[12] *See* Letter Regarding Return on Equity https://dms.psc.sc.gov/Attachments/Matter/a855506d-5fd4-44c8-94c1-a6782297884d.

Commission approve a ROE of 10.5%. See, Application of Duke Energy Carolinas, Para. 24 (Nov. 8, 2018).

Mr. Hevert used a variety of methodologies in his analysis, including two forms of the Discounted Cash Flow ("DCF") model, the Capital Asset Pricing Model ("CAPM"), and the Bond Yield Plus Risk Premium approach. Tr. p. 1787-5, ll. 7-9. Mr. Hevert testified that in formulating his recommended ROE, he also considered a number of other factors to include: (1) the risks associated with certain aspects of the Company's generation portfolio; (2) the Company's significant capital expenditure plan; (3) the risk associated with severe weather; (4) the risk associated with the Company's regulatory environment; and (5) the cost of issuing common stock. In his Rebuttal Testimony, Mr. Hevert updated many of his analyses with data current as of February 15, 2019.

Mr. Hevert acknowledged under cross examination that DEC is, in fact, a less risky company today than it was in 2014 when this Commission granted a 10.2% ROE. Tr. p. 1843, ll. 17-22. Mr. Hevert's testimony urges the Commission to conclude that DEC, although financially sound and one of the largest electric utility companies in the United States, should be viewed as a somewhat risky investment, thus justifying his high ROE recommendation. None of the DEC witnesses, however, claimed at any point in the presentation of the Company's case that DEC is on unstable financial footing or has any particular or unique risk not typically encountered by other electric utilities.

Both ORS witness Parcell and DEC witness Hevert presented detailed testimony regarding the methodologies and models each used to reach their recommended appropriate rate of return and ROE. However, ORS urges the Commission to discount Mr. Hevert's recommended ROE of 10.75%. Despite his recommendation, the Company only requested a 10.50% ROE in its

Application. The Company itself thus appears to have little confidence in being able to justify Mr. Hevert's unusually high recommendation. That Mr. Hevert's methodology produces a 10.75% ROE recommendation that is far out of line with what is being awarded around the country. *See*, Hrg. Ex. 26, DCP-2, Schedule 3.

Walmart witness Tillman testified that the average of the one hundred and eleven (111) reported electric utility rate case ROEs authorized by state regulatory commissions to investor-owned electric utilities from 2016 to date is 9.61%. Tr. p. 1519-15, ll. 3-6 and See, Exhibit GWT-4. Further, Tillman cited SNL Financial data that shows the average ROE for vertically-integrated utilities authorized from 2016 to present is 9.76%, and that annual average authorized ROEs are trending downward. Tr. p. 1519-15, ll. 12-14. See, Hrg. Ex. 53 and 54. This 9.76% average is the basis for ORS's "Plan B" proposal of March 25, 2019.

ORS witness Parcell testified that he has provided testimony as a ROE and Cost of Capital expert witness on several occasions before this Commission since the early 1980s. Tr. p.1178-2, ll. 4-6. He further stated that he has testified in over 570 utility proceedings in approximately 50 regulatory agencies across the United States and Canada. Tr. p. 1178-1, l. 20 - p. 1178-2, l. 2.

In calculating his recommended Cost of Capital and ROE, Mr. Parcell used the hypothetical capital structure of 47 % long-term debt and 53 % common equity, which DEC witness Sullivan described as the "optimal" capital structure for the Company. Tr. p.1178-3, ll. 6-10. To determine the imbedded cost of debt rate, Mr. Parcell updated the Company's proposed cost of debt (i.e., 4.63% as of December 31, 2017) by considering the replacement of three long-term debts that were scheduled to expire in 2018 with four (4) new long-term debts issued in the same year. The resulting cost of long-term debt originally proposed by Mr. Parcell was 4.44%. In his Rebuttal Testimony, DEC witness Sullivan stated the Company did not oppose ORS witness Parcell's

updating the cost of debt but proposed using the actual cost of long-term debt as of December 31, 2018. This cost of debt (i.e., 4.53%) is the imbedded cost of debt rate used by Mr. Parcell in his final Cost of Capital analysis.

To determine a fair and reasonable rate of return, Mr. Parcell estimated an appropriate ROE for the Company. In both his Direct and Surrebuttal Testimonies, Mr. Parcell employed three (3) recognized methodologies to estimate DEC's Cost of Equity: the DCF, CAPM, and Comparable Earnings (CE) models. He applied each of these methodologies to two (2) proxy groups – his own and the one developed by DEC witness Hevert – to establish an ultimate range of 9.1% to 9.5%, with a 9.3% mid-point. Tr. p.1178-4, l.2. Mr. Parcell established this range based on the results of his DCF (range of 9.0% to 9.2% with a 9.1% midpoint) and CE (range of 9.0% to 10.0% with a 9.5% midpoint) models. As a result of these analyses, Mr. Parcell recommended a Cost of Capital in the range of 6.95 to 7.17 %, with a mid-point of 7.06 %. Tr. p. 1178-3, l. 1.

In reaching his recommendation of a 9.3% ROE, Mr. Parcell in large part relied on the DCF model, which is an analysis of current market conditions. The DCF model relies on current stock prices in the marketplace and has traditionally been regarded by this Commission as the best indicator of the return investors require in the marketplace for investment-grade regulated utility companies. Mr. Parcell relied on the results of both his DCF and CE analyses to determine his ROE recommendation and did not include the results of his CAPM analysis as the resulting range (i.e., 6.3% to 6.6%) was too low to be reasonable. Tr. p. 1178-4, l.1-6.

Throughout his Direct and Surrebuttal Testimonies, Mr. Parcell stated that Mr. Hevert's analyses show a consistent pattern of choosing data and methodologies that result in the highest Cost of Equity conclusions. In other words, the data used by Mr. Hevert is intentionally filtered to produce an inflated ROE recommendation to the benefit of the Company. Mr. Parcell further

asserted that Mr. Hevert's use of several "factors" to create more risk for DEC are all factors that are already considered by the rating agencies. In short, Mr. Parcell believes that Mr. Hevert is essentially double-counting risk to, again, artificially inflate his ROE recommendation. Tr. p. 1178-57, l. 15 – p.1178-58, l. 2.

As with Walmart witness Tillman's testimony, Mr. Parcell's ROE recommendation is further supported by authorized ROEs nationwide. Mr. Parcell provided evidence that, from 2017 to 2018, ROEs allowed by regulatory jurisdictions across the country for all electric utilities averaged 9.59% with a median ROE of 9.58%. See, Hrg. Ex. 26, DCP-2, Schedule 3. This national average is only 29 basis points higher than Mr. Parcell's recommendation, but 116 basis points lower than Mr. Hevert's recommended 10.75% ROE. Testimony and supporting materials submitted to the Commission in this proceeding confirms a decline in ROEs across the country in recent years, supports the strength of market conditions, and indicates anticipated upward trend in interest rates in the near term. Coupled with the fact that Mr. Hevert's recommendation of a 10.75% ROE in the present case is an increase over the recommendation that he made to this Commission in Docket No. 2017-370-E just four months ago, it is abundantly apparent that Mr. Hevert's ROE recommendation is extremely misaligned and biased in the Company's interest. These facts call into question the validity of his analyses.

While Mr. Parcell was extensively criticized by Mr. Hevert for his application of the CAPM, as noted above, Mr. Parcell did not use his CAPM analysis in formulating his recommended ROE in this case. Tr. p. 1787-57, l. 16 - p. 1787-60, l. 4. By only using the DCF and CE analysis to produce his recommended ROE, and excluding his CAPM analysis, Mr. Parcell evidenced his efforts to produce a fair and reasonable recommendation to the Commission. Conversely, DEC witness Hevert recommended that both of his DCF analyses be given little

weight by the Commission, apparently in large part due to their yielding results which he believed to be too low. See, Tr. p.1787-32, Table 5 and P. 1787-32, Table 2. Thus, while Mr. Parcell attempted to be unbiased by discounting his CAPM results, which he judged to be too low, Mr. Hevert chose to discount two (2) methodologies that he also claimed to be too low, thus aiding in his producing an inequitably high ROE. Evaluation of the analyses performed by Mr. Parcell and Mr. Hevert clearly establishes the reasonableness of Mr. Parcell's recommended ROE of 9.3%.

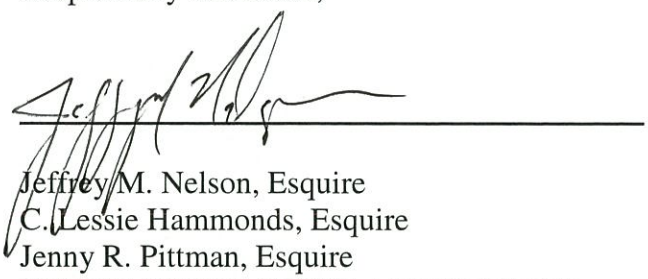
The South Carolina Supreme Court has held that the Commission must determine a fair and reasonable rate of return and must document fully the evidence to justify the rate of return which they award. *Heater of Seabrook, Inc. v. Pub. Ser'v Comm'n of S.C.*, 324 S.C. 56, 64, 478 S.E.2d 826, 830 (1996) citing *Nucor Steel v. S.C. Pub. Ser'v Comm'n*, 312 S.C. 79, 439 S.E.2d 270 (1994). In the present case, the Commission has received extensive testimony from both ORS witness Parcell and Walmart witness Tillman that supports the Commission's finding a fair and reasonable ROE of 9.76%, as proposed by ORS in its "Plan B" filed with the Commission on March 25, 2019 and which is within Mr. Parcell's total ROE range of 9.0% to 10.0%. While ORS witness Parcell's testimony clearly established the propriety of finding of a 9.3% ROE appropriate for this proceeding, a ROE of 9.76% is not only fair and reasonable and based on the evidence in the record, but it is also a reasonable and fair compromise between the calculations of witnesses Parcell and Hevert.

## IV. CONCLUSION

ORS presented reliable and substantial evidence to support a decision by the Commission in adopting ORS's recommendations. ORS respectfully requests this Commission allow DEC to increase BFCs to recover *no more than* 25% of any approved revenue increase assigned to residential TOU, residential non-TOU, and SGS rate classes; disallow a return on deferred O&M

expenses and approve ORS's proposed amortization periods for accounting deferrals; disallow recovery $2,399,000 in O&M expenses; disallow Company adjustments for inflation, growth projections, forecasts, and estimates; disallow recovery of $15,428,000 in bonuses; disallow recovery of $469,894,472 in incremental costs related to CAMA on a system-wide basis to be allocated proportionately to South Carolina; disallow DEC to earn a return on pre-construction costs associated with the cancelled Lee Nuclear Project; disallow recovery of a reserve for an End of Life Nuclear Fund; adopt ORS's proposed amortization periods for Carolinas West Control Center of thirty (30) years, for Lee Combined Cycle of thirty-nine (39) years, and for SC AMI of fifteen (15) years; disallow recovery of $575,000 in legal fees associated with coal ash litigation; allow $1,399,000 in rate case expenses, disallow $2,000,000 in projected rate case expenses, and disallow $512,000 of unsupported rate case expenses; approve a 9.3% ROE.

Respectfully submitted,



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